

UNITED STATES OF AMERICA  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

Before Commissioners:

Ruth Y. Goldway, Chairman;  
Nanci E. Langley, Vice Chairman;  
Mark Acton;  
Mark Hammond; and  
Robert G. Taub

Section 407 Inquiry

Docket No. PI2012-1

NOTICE PROVIDING OPPORTUNITY TO COMMENT  
ON DEVELOPMENT OF COMMISSION VIEWS  
PURSUANT TO 39 U.S.C. 407(c)(1)  
(Issued July 31, 2012)

**REPLY COMMENTS OF FEDERAL EXPRESS CORPORATION**

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Federal Express Corporation (FedEx) greatly appreciates the opportunity granted by the Postal Regulatory Commission (the Commission) to file reply comments in this important docket relating to the Universal Postal Union (UPU) pricing schemes. We will briefly address certain points raised in the other filings.

First, it would be useful to clarify what we are talking about in this docket. FedEx submit that the questions are not limited to terminal dues, which are the rates for letter-mail items, but also the inward land rates. We would anticipate that there might be some debate about the latter, since the Convention does not “establish” those rates, but delegates the fixing of those rates to the Postal Operations Council (POC) in Article 34 of the Universal Postal Convention (the Convention). Parcels are an important element of the global market in international delivery services for both public and private operators. We would argue that the Commission should at the very least conclude that the delegation of price fixing authority to a group of competitors with significant market power does not meet its standards for the establishment of rates, because

there appears to be no process or standards for such rate fixing and no evidence of serious attempts at cost coverage.<sup>1</sup>

Additional, the U.S. Postal Service (USPS) argues in its pleading (at 3-4 and fn 2) that the only thing for the Commission to consider is inbound rates, since the outbound rates are merely “supplier costs.” It is interesting that USPS makes this argument early in its pleading, and then spends pages thereafter complaining about the possible effect of terminal dues on outbound rates. However, FedEx will accept USPS’ limitation of the Commission’s remit and would suggest that any arguments or consideration regarding outbound rates or the effect of terminal dues upon such rates are irrelevant and outside the terms of this proceeding.

Public Representative . FedEx agrees with the Public Representative (PR) that the Commission should stick with its long-standing position that inbound terminal dues fail the cost coverage test. This means the pricing does not comply with the requirement of § 3622(c)(2) that products must cover their costs. This factor, overlooked in the USPS filing, is the only one that is styled as a requirement, and should be the Commission’s major concern.

This is an issue that the Commission has rightly been emphasizing with USPS for some time, as outlined in the PR’s filing. However, we believe that the Commission must do more in its advice to the State Department than comment on the lack of cost coverage. We believe that the Commission must inform the State Department that the inbound rates are not “consistent with the standards and criteria established by the Commission,” 39 USC §407(c)(1). It should also

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<sup>1</sup> In fact, in its document on parcels, the POC says: “The current inward land rates (ILR) system is based on member countries’ 2004 ILRs, with rates effectively frozen from that date, and possible restricted adjustment for inflation on a yearly basis. This has resulted in a pricing system that is relatively simple but also unlikely to be cost-based, and [*sic*] to high per-kilo and per-item rates. It is also inflexible in responding to market conditions and to the changes that need to be made to network cost structures in order to support the UPU parcels service.” 25<sup>th</sup> UPU Congress - Doc 21, “Parcels,” Report by the Postal Operations Council, at 5.

indicate what amendments must be made or reservations offered in order make the Convention consistent with the standards and criteria of Section 3622. This is the role that the Commission is to play under this statute, not that merely as one offering views which can be modified by or ignored by the Secretary, absent overriding foreign policy or national security concerns. The Commission is the expert on fair and proper pricing under U.S. law, and the proposed inbound rates do not meet the most basic of the statutory requirements.

International Mailers Advisory Group. IMAG's comments focus on outbound pricing and therefore might be considered to be irrelevant to the subject of this docket. However, it is important to take their views into consideration after proper analysis, since they represent some major international mailers. What they are saying is that they operate in a "very difficult global market" – which we all do, of course – and that the Commission should therefore allow their prices to be subsidized by domestic mailers and mailers in other countries. While we empathize with all businesses which are under cost constraints, that is not a reason – standing alone – to ignore the problems with the terminal dues and inward land rate systems. These prices are set by collusion (or "consensus," a more palatable but somewhat inaccurate word used by IMAG). When the purpose of such collusion is to allocate market share – which is a description of the UPU pricing systems – it may prove to be beneficial to one group of customers, but that is not a reason to say that those prices are acceptable under applicable legal principles.

USPS. Like the mailers, USPS is quite rightly concerned with its financial situation, which concern it states repeatedly:

In summary, an increase in terminal dues for letter post mail in the Convention will in most circumstances have an overall adverse financial effect on the Postal Service and its operations. Simply put, proposals that have the

effect of increasing terminal dues payments will have an adverse financial impact on the Postal Service. USPS, at 11 (emphasis added).

Like the mailers, they believe that the ends justify the means, in this case the end being that USPS can once again avoid having to adjust or negotiate fairer, more cost-based pricing with post offices in developed countries, at least for the next six years. And USPS is so anxious about changing its agreed-upon pricing system that it uses this pleading to state that a change affecting the system from 2018 until 2012 (which might result from a study proposed by a group of developed countries in Proposal 81) will create “drastic” changes in mailing rates. At the same time, USPS acknowledges that rates that far out in time are “difficult to estimate.” USPS at 7 and at fn 3.

USPS does give passing reference to adverse effects on the “mailing community (the general public and other larger mail users)” in addition to emphasizing the effect on its own finances. USPS at 7. It ignores the possibility of the distortive effect on the global marketplace and on competitors. It also ignores the applicability (as of 2006) of the U.S. antitrust laws to its activities and those of other Federal agencies acting on its behalf (now in the law at 39 USC §409(e)(1)), which has already participated in “numerous terminal dues meeting over the past four years” at which this price fixing scheme was adjusted by the DO’s. USPS dismisses domestic postage (USPS at 9) as a proxy for cost-based pricing, but it then uses that as the defense against the attack on terminal dues as not being cost-based (“a best-fit linearization of 15 domestic rates collected by the International Bureau”), USPS at 14. Overall, we find the USPS lacks the sound legal and economic foundation needed in a discussion of national postal policy guidelines for the broad market in international postal and delivery services.

USPS wants to be participating actively in today's competitive market. It has gotten permission from the Commission to treat much of its international offerings as "competitive products" under 39 USC §3642, and thus now has significant pricing flexibility. At the same time, it wants to continue participating in the historic cartel which has traditionally been "justified" by the DO's public utility-type function. It claims the urgent need to retain the rigid UPU pricing scheme for at least the next nine years. If it is to be permitted to act like a competitor, it must abide by the rules and regulations applicable to actors in the competitive marketplace. It is for that reason that Congress explicitly applied the antitrust laws to its activities. The Commission has said that the cost coverage rule is intended to avoid predatory pricing.<sup>2</sup> USPS needs to step back and figure out how to achieve that.

What is completely beyond our understanding is the strident opposition even to studying changes, with reference to competition laws around the world, represented in Proposal 81. In fact, USPS has purportedly set forth the impact of Proposal 81 as if it were in effect now, while saying essentially that any analysis of its effects is highly speculative. In addition to advising the State Department that the Convention's pricing scheme is not consistent with U.S. postal law, the Commission should urge the State Department to strongly support this study. Such a study could push the rest of the UPU into the modernizing the UPU pricing system among all the major postal operators and thus applying the rules of fair competition in the marketplace equally to both major public and private operators.

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<sup>2</sup> Order Reviewing Competitive Products' Appropriate Share Contribution to Institutional Costs, Docket No. RM2012-3, issued August 23, 2012, at [http://www.prc.gov/Docs/85/85017/Order\\_1449.pdf](http://www.prc.gov/Docs/85/85017/Order_1449.pdf)

James I Campbell, Jr. Mr. Campbell's comments go a long way toward untangling the Gordian knot of terminal dues and exposing its anti-competitive core. However, he admits his work is based on estimates, since the public does not have access to many of the data on the global postal flows. What is clear to us is that his paper demonstrates how dramatically distortive terminal dues are. Even USPS acknowledges that conclusion, indirectly, in explaining how much adapting to true cost-based pricing could cost in terms of price increases. If prices are that far from true costs, then the only conclusion is that significant cross-subsidies and predation must be occurring under the present system.

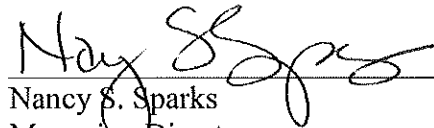
We would strongly urge the Commission to use its own significant economic analytic resources to check on his analysis before coming to its own conclusion – as they say, measure twice and cut once. In our view, pairing Mr. Campbell's study with the Commission's own analysis will reveal how far the UPU system deviates from the Commission's statutory guidelines on fair and proper pricing.

Mr. Campbell makes a much more sophisticated analysis of antitrust concerns that FedEx also raised in its initial filing. We would simply commend to the Commission that portion of his filing, and remind the Commission of the applicability of the U.S. antitrust laws to USPS and other Federal agencies. This legislative provision represents a specific Congressional mandate for policy-makers to help USPS avoid engaging in anything that might be viewed as activity not permitted to a private competitor or group of competitors. We would also commend consideration of the filing by the Nordic operators and the accompanying legal opinion on European Union competition law.

Mr. Campbell also makes significant procedural arguments, which the Commission must consider seriously. This proceeding is an important regulatory initiative and we would expect to see a public order with a fully-stated rationale emerge from it, not a private opinion passed to the State Department without benefit of any administrative-law sunshine. Such an order would also be instructive to other nations, which may be trying to decide whether they can once again allow their designated operators to participate in an anti-competitive system. The United States should be a leader in bringing the processes of the UPU into the 21st century on both governmental and operational fronts. Many of the UPU DO's already have the freedom to operate in this century's competitive markets, so it seem most appropriate that the UPU's structure should be adapted to comply with the competition law requirements that attach to those privileges.

Respectfully submitted,

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